ECONOMIC COMMENTARY

Capital Investment In Alberta To Decline Again In 2016

July 8, 2016

Highlights:

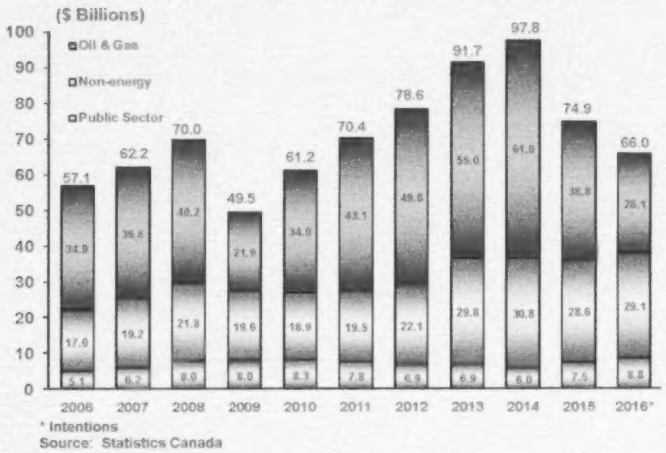
Capital investment was the largest contributor to Alberta's economic growth between the mid-nineties and 2014. However, low oil and gas prices resulted in declining capital investment in Alberta in 2015 and capital investment is expected to remain a drag on economic growth this year as energy investment continues to decline.

Alberta Government

Of the three largest components of Alberta's Gross Domestic Product (GDP), household consumption, international exports and gross fixed capital formation (or capital investment), investment has had the largest impact on Alberta's economic performance since the mid-nineties. Whereas in the 1980's and early 1990's international exports drove the Alberta economy, between 1996 and 2008, capital investment accounted for 70% of Alberta's overall GDP growth, and it was also by far the largest contributor to Alberta's large GDP decline in 2009 and to its subsequent recovery. Between 2009 and 2013, capital investment accounted for 82% of Alberta's total GDP growth. However, in 2014 investment made only a small contribution to Alberta's overall GDP growth and it has declined sharply since then because of the downturn in the oil and gas sector that was driven by lower oil and gas prices.

Statistics Canada has recently released preliminary capital investment estimates for 2015 and investment intentions for 2016 from its Capital and Repair Expenditures Survey. Investment includes capital spending on both construction and machinery and equipment reported by private and public organizations, but excludes residential investment.

Chart 1
Non-Residential Investment In Alberta



* Intentions
Source: Statistics Canada

In 2015, capital investment in Alberta fell sharply by 23.4% to $74.9 billion from 2013, following an increase of 6.7% in 2014. Construction spending, which accounted for 71% of total investment spending, declined by 27.7% while spending on machinery and equipment fell 10.4%. Following an 8.7% increase in 2014, private investment was down 26.6% in 2015 to $82.4 billion. Public investment was up 13.9% to $8.8 billion in 2015.

The sectors with the highest investment growth in 2015 were:

- Arts, entertainment and recreation (up 53.2%);
- Educational services (up 48.4%);
- Culture and information (up 28.9%);
- Public administration (up 27.6%); and
- Real estate and rental and leasing (up 5.3%).

However, most other sectors had lower investment spending in 2015 than in 2014, led by a 37.5% drop in the oil and gas extraction sector due to much lower oil and gas prices. The sectors with the largest investment declines in 2015 were:

- Oil and gas extraction (down 37.5%);

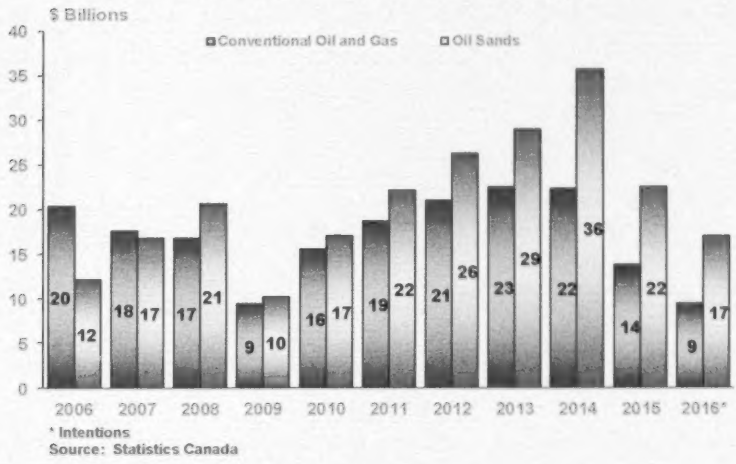
- Professional, scientific and technical services, such as engineering services (down 28.3%);
- Utilities (down 25.2%);
- Health care and social assistance (down 23.6%); and
- Wholesale trade (down 20.3%).

Investment spending in the manufacturing sector rose 1.4% as sharp declines in the wood products, pulp and paper, chemicals and food and beverage sectors were more than offset by strong growth in the refined petroleum products, non-metallic minerals and fabricated metals sectors.

The oil and gas sector's investment spending was estimated to have decreased by 36.4% to $38.7 billion from 2014, accounting for 52% of total capital investment in Alberta. This sector is an important contributor to capital investment in Alberta and oil and gas prices play a critical role in the investment in this sector.

During Alberta's first investment boom, which lasted from 1996 to 2008, the value of capital investment spending quadrupled. Oil and gas prices rose strongly over that period which led to surging investment in the energy sector, especially in the oil sands. Oil sands investment was also impacted by technological breakthroughs, such as the Steam-Assisted Gravity Drainage process. The wealth effects of higher energy prices also spilled over onto other sectors, such as transportation (especially pipelines), manufacturing (especially fabricated metals and machinery) and public institutions (especially provincial government, education and healthcare).

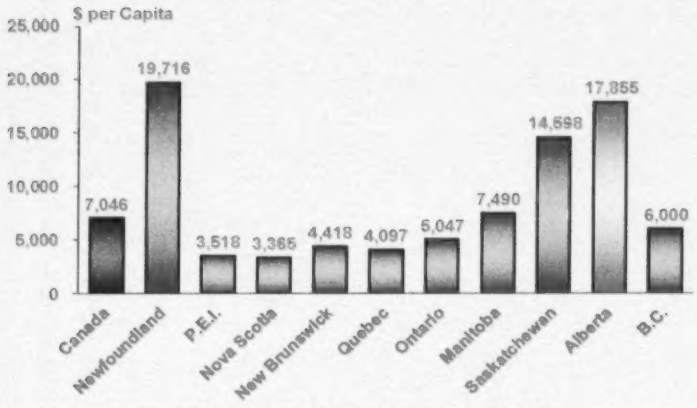
Chart 2
Oil and Gas Capital Investment in Alberta



* Intentions
Source: Statistics Canada

Within the oil and gas sector, investment in conventional oil and gas projects more than doubled between 1996 and 2008 to $16.8 billion while oil sands investment reached $20.6 billion in 2008 (Chart 2), twenty times as high as in 1996. During the global recession of 2009, total investment spending fell by 29.2%, and oil and gas investment by 47.4% as many previously announced large projects were put on hold. Investment bounced back strongly after 2009 and by 2014 investment spending had reached new highs, as oil and gas investment nearly tripled during those five years. However, total mining and oil and gas investment fell sharply by 36.4% in 2015 because of that sector's downturn which was caused by sharply lower oil and gas prices. Oil sands investment was estimated to have dropped by 37% to $22.5 billion, while conventional oil and gas investment fell 38.3% to $13.8 billion and investment spending by oil and gas service companies declined 12.5% to $2.4 billion.

Chart 3
Per Capita Investment in 2015



Sources: Statistics Canada and Alberta Economic Development and Trade

In 2015, Alberta's per capita capital spending was the second highest of all provinces at $17,855; two-and-a-half times the Canadian average of $7,046 per capita and second only to Newfoundland and Labrador's $19,716. Alberta accounted for 30% of total capital investment in Canada in 2015.

In 2016, due to continued weakness in oil and gas prices and suspensions and delays of projects in the oil and gas extraction industry, non-residential capital spending in Alberta is anticipated to drop by 11.9% or $8.9 billion from 2015 to $66.0 billion. Construction spending is forecast to drop by 9.9% and machinery and equipment spending by 16.6%. Private investment is expected to decline by 16.2% but public investment is anticipated to rise 20.6%.

Capital expenditures by conventional oil and gas companies are expected to drop by 31.3% to a seven-year low of $9.5 billion in 2016 and expenditures by oil sands companies are expected to decline by 24.5% to a seven-year low of $17.0 billion. This forecast is so far borne out by the first quarter results of the Quarterly Survey of Capital Expenditures – Oil and Gas Activities: capital spending by Canadian oil and gas extraction firms fell to $10.7 billion, down 31% from a year earlier and down sharply from the $22.2 billion registered in the fourth quarter of 2014. (Alberta accounts for about three-quarters of Canadian oil and gas spending.) Investment by organizations providing support services to mining and oil and gas extraction industries, such as rigging and drilling, is anticipated to drop by 36.3% in 2016 to $1.5 billion.

Other sectors anticipating decreases in capital spending include: administrative and waste management services (down 36.2%); arts, entertainment and recreation (down 11.7%); and professional, scientific and technical services (down 9.8%).

Sectors which anticipate high growth in 2016: federal government (up 101.5%); education (up 63.0%); wholesale trade (up 10.8%); transportation and warehousing (up 8.6%); and information and culture (up 8.4%).

In summary, capital investment spending in Alberta declined sharply in 2015 as oil and gas extraction companies have slashed investment spending because of low oil and gas prices. Investment is forecast to decline again in 2016 because of another sharp contraction in spending by the oil and gas sector. Even with last year's decline Alberta's per capita investment spending still far exceeded the Canadian average in 2015.